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SUPREME COURT OF THE UNITED STATES

OCTOBER TERM 1932

No. 627

PUBLIC SERVICE COMMISSION OF MONTANA, et al.,

Appellants,

vs.

GREAT NORTHERN UTILITIES COMPANY,

Appellee.

Appeal from the District Court of the United States, in and for the District of Montana.

Brief for Appellee

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INDEX

	Page
Order violative of due process of law clause of 14th Amendment	1
Argument and Authorities	2
Order invalid in depriving Appellee of right of competition	2
Order invalid in prescribing minimum rates	12
Order invalid because Commission did not apply principle of a fair return	28
Order invalid for reason not supported by evidence before or findings made by Commission	31
Order invalid for reason not made in public interest	33
Rates prescribed by order do not furnish Appellee with a fair return	35
Sufficiency of Complaint	38
Contention that franchise contract precludes Appellee from challenging rates	40
Sufficiency of Findings of Trial Court	41

TABLE OF CASES

Addyston Pipe & Steel Co. v. United States, 175 U.S. 211	24
Atchison T. & S. F. Ry. Co. v. I C. C., 190 Fed. 591	30
Atlantic Coast Line Co. v. Trammell, 287 Fed. 741	30
Billings v. United States, 232 U.S. 261	22
Board of Public Utility Comrs. v. N. Y. Telephone Co., 271 U.S. 23	9, 29
Bluefield W. W. & Imp. Co. v. Public Service Commission, 262 U.S. 679	29
Brushhaber v. Union P. R. Co., 240 U.S. 1	21
Budd v. State of New York, 143 U.S. 517	19
Coppage v. Kansas, 236 U.S. 1	28
Cotting v. Goddard, 183 U.S. 79	19
Dayton-Goose Creek R. Co. v. U.S., 263 U.S. 456	26
Den v. The Hoboken Land and Imp. Co., 18 Howard (U.S.) 272	13
Dow v. Beidelman, 125 U.S. 680	19

TABLE OF CASES—(Continued)

	Page
Fitchburg R. R. Co. v. Gage, et al, 12 Gray (Mass.) 393	20
Ga. Ry. & Power Co. v. R. R. Commission, 262 U.S. 625	9
Great Northern Utilities Co. v. Public Service Commission, 52 Fed. (2d) 802	10, 38, 39
Great Northern Utilities Co. v. Public Service Commission, 88 Mont. 180	11
Gibbons v. Ogden, 9 Wheaton 1	23
Interstate Commerce Commission v. Chicago G.W.R. Co., 209 U.S. 108	7, 18
Johnson v. Pensacola etc. R. R. Co., 16 Fla. 623	20
Lochner v. N.Y., 198 U.S. 45	27
Lough v Outerbridge, 143 N.Y. 271	19
Martin v. Hunter's Lessee, 1 Wheaton 304	25
McCardle v. Indianapolis Water Co., 272 U.S. 400	35
Munn v. Illinois, 94 U.S. 113	13, 14, 15, 16, 17
Northern P. R. Co. v. Department of Public Works, 268 U.S. 39	33
Prout v. Starr, 188 U.S. 537	22
Skinner & Eddy Corp. v. United States, 249 U.S. 557	18
Smith v. Illinois Bell Telephone Co., 282 U.S. 133	40
Southern Pac. Co. v. I.C.C., 219 U.S. 433	30
Tagg Bros. & Moorhead v. U.S., 280 U.S. 420	30
Texas Elec. Service Co. v. City of Seymour, 54 Fed. (2d) 97	10
Tyson & Bro. v. Banton, 273 U.S. 418	27
Wilson v. New, 243 U.S. 332	25
Wolff Packing Company v. Court of Industrial Relations, 262 U.S. 522	25

TEXT BOOKS

Cooley on Constitutional Limitations, Seventh Ed., page 9	25
Cooley on Constitutional Limitations, Seventh Ed., page 124	12
Corpus Juris, Vol. 10, page 420	7

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Brief for Appellee

The order in question is violative of the due process of law clause of the 14th Amendment for the reasons:

1. The effect of said order is to deprive appellee of the right of competition in rates essential to pro-

tection and preservation of its property and business.

2. The order deprives appellee of the right to charge rates concededly less than reasonable rates.

3. The Commission in making said order did not apply the principle of a fair return but adopted an erroneous rule of law.

4. The order is not supported by the evidence introduced before or by the findings of the Commission.

5. The order was not made in the interest of the public but in the interest of the Citizens Gas Company.

6. The rates prescribed by said order are insufficient to furnish appellee a fair return.

ARGUMENT AND AUTHORITIES

I.

The order is violative of the due process of law clause of the 14th Amendment in depriving appellee of the right of competition in rates essential to the protection and preservation of its property and business.

The gas system of appellee had been installed pursuant to a franchise granted by the City of Shelby and was in operation about five years before the Citizens Gas Company entered the field as a competitor in October, 1928. The system was designed and is of

capacity to meet the present and future requirements of the city and its inhabitants and appellee has an ample supply of natural gas (R. 3). The franchise of the Citizens Gas Company was granted to a local company promoted by the citizens of Shelby and it was the announced intention of the grantee of the franchise to enter into competition with appellee (R. 44). The distribution system of the Citizens Gas Company, at the time of the hearing before the Public Service Commission, covered the business section and a portion of the residential section of the city (R. 44 and 45), but has been extended until it is now substantially a duplication of the system of appellee, as shown by Plaintiff's Exhibit No. 2 (R. 82-A and 82-B).

In October, 1928, when the Citizens Gas Company commenced furnishing gas, the appellee was charging rates approved by the Commission, consisting of a base rate of 50c per M. cubic feet and lower rates for increased consumption. The initial rates of the Citizens Company, approved by the Commission, consisted of a base rate of 35c per M. cubic feet and lower rates for increased consumption. (R. 45).

At the time the Citizens Company commenced operating in the fall of 1928, appellee had 485 customers and within a short time 137 of these customers

became customers of the Citizens Gas Company. (R. 5, 61 and 66).

It was in view of this situation that appellee entered upon what is termed by the Commission a "rate war" and filed with the Commission a proposed schedule of rates designated as "Schedule 4-A." (Tr. 5-6). The dates proposed by this schedule consisted of a rate of 20c per M. cubic feet up to 300,000 cubic feet per month and 15c per M. cubic feet for the excess. (R. 45).

The Citizens Company promptly complained of the rates so proposed on the grounds that the same were "unfair, unjust and unreasonable" to the company and constituted "unjust and unfair" competition. (R. 45). A hearing was had by the Commission on December 20, 1928, and at this hearing the Citizens Company and twelve customers (presumably stockholders of that company) were the only protestants against the rates proposed by Schedule 4-A. (R. p. 17).

As a result of the hearing, the Commission found and determined the present value of the system of appellee to be $46,091.72 (R. 62) and that the rates proposed by Schedule 4-A would not yield sufficient revenue to defray normal operating expenses, including a fair allowance for depreciation and were therefore

"unjust and unreasonable," for which reason the Commission refused to approve same upon the theory that it was to the public interest that appellee should earn sufficient to maintain its plant and render adequate service. (R. 69).

The Commission, after having determined that the rates proposed by Schedule 4-A are unjust and unreasonable, prescribed the schedule of rates set forth in the order in question, which were identical with the initial rates of the Citizens Company that had been approved by the Commission.

The system of the Citizens Gas Company was purchased by the citizens of Shelby (R. p. 101). The officers and directors of the Citizens Company were residents of the city of Shelby. The mayor of the city who is also a member of the school board, is president of the company. (R. 100). There are 43 subscribers to the capital stock of the Citizens Company "among the citizens of Shelby" and all but two are customers of said company (R. 102). The City of Shelby has a population, according to the 1930 Federal census, of 2004.

In January, 1930, the Citizens Company made a reduction in rates and adopted a rate of 23c per M. cubic feet, with a discount of 3c if paid on or before the 10th of the month, and this is the rate now being

charged. This rate was submitted to the Commission for approval in March, 1930. The Commission has never made any investigation of the rates of the Citizens Company or the value of its property or of its operation (R. 100-101).

From the table presented in the brief for appellant, (page 91), it appears that the volume of gas sold by appellee has decreased each year since 1928, while the volume of gas sold by the Citizens Company has increased each year. For the first seven months of 1932, the appellee sold 39,559,000 cubic feet of gas, notwithstanding the rate was reduced to 15c per M. cubic feet September 1st, 1931, while, during the same period, the Citizens Gas Company sold 67,599,000 cubic feet. In 1931, appellee sold 55,869,-000 cubic feet, which was less than one-half the amount sold in 1927, before competition began.

The appellee, in September, 1931, adopted a flat rate of 15c per M. cubic feet for the purpose of holding the customers it had and with a view of enlarging its list of customers. The reduction thus made did not have the effect of increasing the number of customers or the volume of sales (R. 96).

In view of these undisputed facts, there can be no doubt that if appellee is required to put into effect the schedule of rates prescribed by the order in question,

its business and property will be of no value whatever, as it would lose all of its customers and its gas system would be valueless, except possibly for a small salvage value.

The earnings of a public utility are not only dependent upon rates, but also upon patronage. Rates which, because of competition, will deprive a utility of its patronage and may ultimately require the utility to abandon the field to a competitor, are as objectionable, from the standpoint of confiscation, as rates which will not furnish a fair return where there is no competition. *The power of regulation does not warrant confiscation, whether resulting from rates unreasonably low or from rates which will deprive the utility of its patronage.*

In 10th Corpus Juris, page 420, it is said:

> "Competition is a very important factor in determining the reasonableness of rates, provided it possesses the attribute of producing a substantial and material effect on traffic and rate making, and may be controlling in relation thereto. Carriers must be allowed to meet competition or they must go out of business."

This court in the case of Interstate Commerce Commission v. Chicago G. W. R. Co., 209 U. S. 108, 119, said:

> "It follows that railroad companies * * * * in fixing their own rates * * * * may take into account competition with other carriers, provided

only that the competition is genuine and not a pretense."

If rates to meet genuine competition are deemed reasonable and lawful, it, of course, follows that a utility cannot be compelled to increase such rates when the increase would result in the loss of its patronage to a competitor. Such increased rates would be unreasonable rates.

The rates proposed by Schedule 4-A were condemned by the Commission because it was found that they would not "even yield enough revenues to defray normal operating expenses, including a fair allowance for depreciation," and it was argued by the Commission that it is to the public interest that appellee should earn sufficient to maintain its plant and render adequate service, (R. 69). It is wholly immaterial so far as the public is concerned whether the failure to maintain the plant and render adequate service is due to lack of earnings because of unreasonably low rates, or to insufficient revenue because of loss of patronage.

Although the rates provided in Schedule 4-A were charged by the appellee from November 1, 1928, to September 1, 1931, when the rate was reduced to 15c per M. cubic feet, (R. 91), there is no evidence that the gas system of appellee has not been properly main-

tained or adequate service furnished. If appellee and its stockholders are willing, as they have been, to maintain the system and furnish gas at these rates, the public is not injured, but, on the contrary, is benefitted by such low rates. The losses willingly suffered by appellee cannot be taken into account in determining reasonable rates for the future.

Public Utilities Commission v. N. Y. Telephone Co., 271 U. S. 23;
Ga. Ry. & Power Co. v. R. R. Commission, 262 U. S. 625.

The only complaint against these rates is by the Citizens Gas Company and its customers. These customers are not affected by these rates and the only interest of the Citizens Gas Company is the private selfish interest of destroying the business and property of its competitor, the appellee, in keeping with its avowed intention when it entered the field.

The trial court found:

> "That the rates prescribed by the Commission for the plaintiff company deprive it of the right of competition, which right plaintiff has in the circumstances disclosed and said rates, if applied to plaintiff's operations, would destroy its property." (R. p. 24).

In the majority opinion of the lower court, on the application for an interlocutory injunction, it is said:

> "When the state launches two upon the sea of

competition, and the plank of patronage will support but one, it cannot in reason deny them the right of necessity to fight to a finish for financial life, even as may two castaways at sea battle to the death for the spar which will support but one, without any wrong to the survivor attaching." (52 Fed. (2d) 802, 805).

If rates to meet genuine competition are deemed reasonable and lawful, it, of course, follows that a utility cannot be compelled to increase such rates when the increase would result in the loss of its patronage to a competitor. Such increased rates would be unreasonable rates.

Texas Electric Service Co. v. City of Seymour, 54 Fed. (2d) 97.

If, as we contend, and as decided by the trial court, the compelling of appellee to increase its rates will have the effect of destroying its business and rendering its gas system valueless, the state statute, if it authorizes this to be done, as argued for appellants, is violative of the due process of law clause of the 14th Amendment.

It is argued for appellants (Appellants' Brief, pp. 50 to 56) that as the Supreme Court of the State has decided that the state statute authorizes the prescribing of precise or minimum rates, the trial court in this case in deciding that the rates prescribed by the

order in question are unreasonable, failed to give effect to the statute of the state as so construed and recognized an unauthorized exception to the statute.

In the opinion of the Supreme Court of the State of Montana in the case referred to,—88 Mont. 180-203, —it is said:

> "The trial court did not consider the testimony adduced at the hearing before the Commission, and no opportunity was offered for the submission of any additional testimony, for plaintiff's motion for judgment on the pleadings was granted. The rates determined upon must be just and reasonable. (Sec. 3899, Rev. Codes 1921). This court does not have before it any testimony whatsoever. What constitutes 'just and reasonable' rates must, of necessity, depend upon the facts in each case. A rate altogether just and reasonable in one instance may be most unjust and unreasonable in another. Not having the facts before us, this court is unable to determine whether the rates fixed are just and reasonable; and therefore we hold that that matter is not before us for consideration."

Whether the rates would have been held reasonable in the light of the record in this case was not before the Supreme Court of the State and as said by that court, "A rate altogether just and reasonable in one instance may be most unjust and unreasonable in another."

II.

The right to charge any rate not discriminatory within the limits of a reasonable rate is a right guaranteed by the due process of law clause of the 14th Amendment.

In determining whether a statute of a state affecting life, liberty or property is violative of the due process of law clause of the 14th Amendment, it is necessary to inquire whether the statute is within the legislative power. If it is within such power, it is not prohibited by this amendment, but if it is not within such power it is within the prohibition of the amendment.

The legislative power of a state must be tested and determined by the principles of the common law because that is the source from whence such power is derived. Mr. Cooley in his work on Constitutional Limitations, Seventh Edition, page 124, says:

> "In considering the powers which may be exercised by the legislative department of one of the American states, it is natural that we should recur to those possessed by the Parliament of Great Britain, after which, in a measure, the American Legislatures have been modelled, and from which we derive our legislative usages and customs, or parliamentary common law, as well as the precedents by which the exercise of legislative power in this country has been governed. It is natural, also, that we should incline to measure the power of the legislative department in

> America by the power of the like department in Britain; and to concede without reflection that whatever the legislature of the country from which we derive our laws can do, may also be done by the department created for the exercise of legislative authority in this country."

In England the legislative power of Parliament was controlled and limited by the provision in Magna Charta declaring that no person shall be deprived of life, liberty, or property, "but by the judgment of his peers or the law of the land." This provision while differing in language from the due process of law clause of the 14th Amendment had the same meaning. In the case of Den v. The Hoboken Land and Improvement Co., 18 Howard (U.S.) 272, the court said:

> "The words 'due process of law,' were undoubtedly intended to convey the same meaning as the words 'by the law of the land,' in Magna Charta. Lord Coke, in his commentary on those words (2 Inst. 50), says, they mean due process of law."

In the Munn case, 94 U. S. 113, in discussing the legislative power of a state, the court said:

> "While this provision of the Amendment is new in the Constitution of the United States as a limitation upon the powers of the states, it is old as a principle of civilized government. It is found in Magna Charta, and, in substance if not in form, in nearly or quite all the constitutions that have been from time to time adopted by the several states of the Union. By the 5th Amendment, it was introduced into the Constitution of

the United States as a limitation upon the powers of the National Government, and by the 14th, as a guaranty against any encroachment upon an acknowledged right of citizenship by the legislatures of the states.

When the people of the United Colonies separated from Great Britain, they changed the form, but not the substance, of their government. They retained for the purposes of government all the powers of the British Parliament and, through their State Constitutions or other forms of social compact, undertook to give practical effect to such as they deemed necessary for the common good and the security of life and property. All the powers which they retained they committed to their respective states, unless in express terms or by implication reserved to themselves. Subsequently, when it was found necessary to establish a national government for national purposes, a part of the powers of the states and of the people of the states was granted to the United States and the people of the United States. This grant operated as a further limitation upon the powers of the states, so that now the governments of the states possess all the powers of the Parliament of England, except such as have been delegated to the United States or reserved by the people. The reservations by the people are shown in the prohibitions of the constitutions."

The court further said:

"This brings us to inquire as to the principles upon which this power of regulation rests, in order that we may determine what is within and what without its operative effect. *Looking, then, to the common law, from whence came the right which the Constitution protects*, we find that when private property is 'affected with a

public interest, it ceases to be *juris privati only*'." (Italics ours).

For the same reason that the court in that case found it necessary to refer to the principles of the common law in determining whether the prescribing of maximum rates was violative of the due process of law clause of the 14th Amendment, it is necessary to consider the common law in determining whether the prescribing of minimum rates is within the legislative power.

In the opinion in the Munn case, the court, after reviewing the English cases, said:

"We have quoted thus largely the words of these eminent expounders of the common law, because, as we think, we find in them the principle which supports the legislation we are now examining. * * * *

In countries where the common law prevails, it has been customary from time immemorial for the legislature to declare what shall be a reasonable compensation under such circumstances, or *perhaps more properly speaking, to fix a maximum beyond which any charge made would be unreasonable.* * * * * The controlling fact is the power to regulate at all. If that exists, the right to establish the *maximum of charge*, as one of the means of regulation, is implied. In fact, the common law rule, which requires the charge to be reasonable, is itself a regulation as to price. Without it the owner could make his rates at will, and compel the public to yield to his terms, or forego the use." (Italics ours).

The common law rule as announced in the English

cases cited and discussed in the opinion in the Munn case requires the rate or charge to be limited to a "reasonable" charge or rate. The whole import of the opinions of the English courts to which reference is made is that the principle of regulation so far as rates or charges are concerned is for the purpose of preventing extortionate or unreasonable charges. It was undoubtedly in view of this fact that the court in the Munn case, in order to correctly state the principle of regulation of rates, as deduced from the English authorities, qualified the statement that the common law authorized the "legislature to declare what shall be a reasonable compensation" by adding the words, "*or, perhaps more properly speaking, to fix a maximum beyond which any charge made would be unnreasonable.*"

We further quote from the opinion in the Munn case as follows:

> "When, therefore, one devotes his property to a use in which the public has an interest, he, in effect, grants to the public an interest in that use, and must submit to be controlled by the public for the common good, to the *extent of the interest he has thus created.*" (Italics ours).

From the briefs as published with the opinion in the Munn case, it appears that it was argued that if the power to regulate charges exists, minimum rates may be prescribed. When, therefore, the court announced its purpose to ascertain the power to regu-

late rates and then defined what is within and what is without the "operative effect" of such power, the statement that the power is limited to the "fixing of a maximum beyond which any charge made would be unreasonable" cannot be otherwise construed than that the power does not embrace the fixing of minimum rates.

In the concluding paragraph of the opinion, it is said:

> "In passing upon this case, we have not been unmindful of the vast importance of the questions involved. This and cases of a kindred character were argued before us more than a year ago by the most eminent counsel, and in a manner worthy of their well earned reputations. We have kept the cases long under advisement, in order that their decision might be the result of our mature deliberations."

It thus appears that the opinion was not one hastily expressed but the result of great deliberation and it must be assumed that every statement made was considered and weighed before the opinion was announced.

But whatever may be said with reference to the Munn case establishing the proposition that the legislative power at common law was limited to the prescribing of maximum rates, in later cases, this court has definitely and positively so decided.

In the case of Skinner & Eddy Corp. v. United

States, 249 U. S. 557, 564, 565, the court in the opinion, referring to the Interstate Commerce Act, said:

> "The original act, proceeding upon the common-law rule which prohibits public carriers from charging more than reasonable rates, gave the Commission power to declare illegal one unduly high; but even after such a determination the Commission lacked the power to fix the rate which should be charged. * * * *
>
> Congress, however, steadfastly withheld from the Commission power to prevent by direct action the charging of unreasonably low rates. *The common law did not recognize that the rate of a common carrier might be so low as to constitute a wrong;* and Congress has declined to declare such a rule. Despite the original Act to Regulate Commerce and all amendments, railroads still have power to fix rates as low as they choose and to reduce rates when they choose." (Italics ours).

In the case of Interstate Commerce Commission v. Chicago Great Western Ry. Co., 209 U.S. 108, 119, the court quotes approvingly from an opinion of the Interstate Commerce Commission as follows:

> "Subject to the two leading prohibitions that their charges shall not be unjust or unreasonable, and that they shall not unjustly discriminate so as to give undue preference or disadvantage to persons or traffic similarly circumstanced, *the act to regulate commerce leaves common carriers as they were at the common law—free to make special rates looking to the increase of their business, to classify their traffic, to adjust and apportion their rates so as to meet the necessities of commerce and of their*

own situation and relation to it, and generally to manage their important interests upon the same principles which are regarded as sound and adopted in other trades and pursuits." (Italics ours).

After thus quoting, the court in the opinion said:

"It follows that railroad companies * * * * in fixing their own rates, they may take into account competition with other carriers, provided only that the competition is genuine, and not a pretense."

The decision in the Munn case as to the limitations of legislative power in regulating rates has been accepted and followed in all subsequent cases by this court and in defining the power the court has uniformly limited it to the fixing of maximum rates.

Budd v. State of New York, 143 U. S. 517, 36 L.Ed. 246;
Dow v. Beidelman, 125 U. S. 680, 31 L.Ed. 841;
Cotting v. Goddard, 183 U. S. 79, 46 L. Ed. 92.

While the decision in the Munn case is controlling, we find that other courts have given the same construction or meaning to the common law. In the case of Lough v. Outerbridge, 143 N.Y. 271, the court, in discussing the rights and duties of a common carrier, said:

"When the service is performed for a reasonable and just hire the public have no interest in the question, whether one or many are engaged in it. The monopoly which the law views with

disfavor is the manipulation of a business in which the public are interested in such a way as to enable one or a few to control and regulate it in their own interest, and to the detriment of the public, by exacting unreasonable charges, *but when an individual or a corporation has established a business of a special and limited character, such as the defendants in this case had, they have a right to retain it by the use of all lawful means. That was what the defendants attempted to do against a competitor that engaged in it, not regularly or permanently, but incidentally and occasionally. The means adopted for this purpose was to offer the service to the public at a loss to themselves whenever the competition was to be met, and when it disappeared to resume the standard rates, which, upon the record, did not at any time exceed a reasonable and fair charge. I cannot perceive anything unlawful or against the public good in seeking by such means to retain a business which it does not appear was of sufficient magnitude to furnish employment for both lines.*" (Italics ours).

See also:

Fitchburg R. R. Co. v. Gage, et al, 12 Gray (Mass.) 393;
Johnson v. Pensacola, etc. R. R. Co., 16 Fla. 623, 26 Am. Rep. 731.

We concede that the Interstate Commerce Commission has power to prescribe minimum rates by virtue of the Transportation Act of 1920. In other words, the power was legally conferred, notwithstanding the due process of law clause of the 5th Amendment to the Federal Constitution.

In determining the question of whether the statute of a state violates the due process of law clause of the 14th Amendment, it is necessary to determine what is within and what without such legislative power from a consideration of the common law as we have already pointed out. In determining whether an act of Congress violates the due process of law clause of the 5th Amendment, it is only necessary to inquire whether Congress has exercised a power granted by the Federal Constitution. If the power has been granted, of course, there can be no conflict with the 5th Amendment, which became effective in 1798 or several years after the adoption of the Constitution.

Among the powers granted to Congress by Article I of the Federal Constitution is the power "to regulate commerce with foreign nations, and among the several states, and with the Indian tribes." It was by virtue of this power that the Transportation Act of 1920 was enacted.

If then this power to regulate authorizes the prescribing of minimum rates, it follows that the Transportation Act is not violative of the 5th Amendment. As said in the case of Brushhaber v. Union P. R. Co., 240 U. S. 1, 24, which involved the taxing power of Congress:

"the Constitution does not conflict with itself

> by conferring, upon the one hand, a taxing power, and taking the same power away, on the other, by the limitations of the due process of law clause."

This observation, of course, is equally true with reference to the power to regulate commerce.

In the case of Prout v. Starr, 188 U. S. 537, 543, it is said:

> "The Constitution of the United States, with the several amendments thereof, must be regarded as one instrument, all of whose provisions are to be deemed of equal validity. It would, indeed, be most unfortunate if the immunity of the individual states from suits by citizens of other states, provided for in the 11th Amendment, were to be interpreted as nullifying those other provisions which confer power on Congress to regulate commerce among the several states," etc.

In the case of Billings v. United States, 232 U. S. 261, 282, the court said:

> "It is also settled beyond dispute that the Constitution is not self-destructive. In other words, that the powers which it confers on the one hand it does not immediately take away on the other; that is to say, that the authority to tax which is given in express terms is not limited or restricted by the subsequent provisions of the Constitution or the Amendments thereto, especially by the due process clause of the 5th Amendment."

The 5th Amendment in no manner affected the powers granted Congress by the Constitution. The effect of the amendment was to limit and confine

Congress to the proper exercise of the powers granted. In this respect the 5th Amendment has the same effect upon Congress that the 14th has upon the legislatures of the states.

It is true that in the opinions of this Court we find expressions to the effect that the due process clause of the 5th Amendment has the same meaning as the due process clause of the 14th Amendment, as both are couched in the same language. The court, however, did not by these statements intend to say that whatever legislation is within the powers of Congress is also within the legislative power of a state. The two amendments have the same meaning in that they are both restraints upon legislative power,—one, the legislative power of Congress, and the other the legislative power of a state. They cannot and do not have the same meaning in the respect that whatever Congress may do in the exercise of legislative powers granted by the Constitution may also be done by a state in the exercise of its legislative power.

In the case of Gibbons v. Ogden, 9 Wheaton 1, 196, Chief Justice Marshall defined the power to regulate commerce as follows:

> "It is the power to regulate; that is, to prescribe the rule by which commerce is to be governed. This power, like all others vested in Congress, is complete in itself, may be exercised to

its utmost extent and acknowledges no limitations, other than are prescribed in the Constitution."

Whatever the power of Congress to regulate commerce before the adoption of the 5th Amendment included, it includes now. The 5th Amendment to no extent curtailed this power.

In the case of Addyston Pipe & Steel Co. v. United States, 175 U. S. 211, 229, the court in referring to the 5th Amendment, said:

> "*The provision in the Constitution does not, as we believe, exclude Congress from legislating with regard to contracts of the above nature while in the exercise of its constitutional right to regulate commerce among the states. On the contrary, we think the provision regarding the liberty of the citizen is, to some extent, limited by the commerce clause of the Constitution,* and that the power of Congress to regulate interstate commerce comprises the right to enact a law prohibiting the citizen from entering into those private contracts which directly and substantially, and not merely indirectly, remotely, incidentally, and collaterally, regulate to a greater or less degree commerce among the states." (Italics ours).

When it is considered that there is no common law of the United States, and that the Constitution of the United States emanated from the people who were in no manner limited in granting powers to Congress, whereas the states can only exercise the legislative power recognized and sanctioned by the common law,

it must follow that the legislative powers of Congress cannot be measured by the legislative power of a state or vice versa.

In the case of Martin v. Hunter's Lessee, 1 Wheaton, 304, 324, the court, in an opinion by Justice Story, said:

> "The Constitution of the United States was ordained and established, not by the states in their sovereign capacities, but emphatically, as the preamble of the Constitution declares, by 'the people of the United States.' There can be no doubt that it was competent to the people to invest in the general government with all the powers which they might deem proper and necessary; to extend or restrain these powers according to their own good pleasure, and to give them a paramount and supreme authority."

Mr. Cooley, in his work on Constitutional Limitations, Seventh Edition, page 9, in discussing the Federal Constitution, said:

> "As much larger powers were vested by this instrument in the general government than had ever been exercised in this country by either the Crown, the Parliament, or the Revolutionary Congress, and larger than those conceded to the Congress under the Articles of Confederation, the assent of the people of the several states was essential to its acceptance," etc.

In the case of Wolff Packing Co. v. Court of Industrial Relations, 262 U. S. 522, 67 L.Ed. 1103, it was contended that the case of Wilson v. New, 243

U. S. 332, in which it was held that an act of Congress regulating the wages of employees of carriers engaged in interstate commerce was constitutional, was conclusive of the constitutionality of a statute of Kansas authorizing the fixing of wages. The court, in the opinion, said:

> "The minutely detailed government supervision, including that of their relations to their employees, to which the railroads of the country have been gradually subjected by Congress *through its power over interstate commerce, furnishes no precedent for regulation* of the business of the plaintiff in error, whose classification as public is, at the best, doubtful. * * * *
>
> We think the Industrial Court Act, in so far as it permits the fixing of wages in plaintiff in error's packing house, is in conflict with the 14th Amendment, and deprives it of its property and liberty of contract without due process of law." (Italics ours).

In the opinion in the Dayton Goose Creek R. Co. case, 263 U. S. 456, in which the constitutionality of the recapture provision of the Transportation Act of 1920 was sustained, the court discusses the extent of the power of Congress to regulate commerce and states the reasons for the broad and comprehensive power conferred by that Act upon the Interstate Commerce Commission over rates for common carriers. The reasons thus stated can have no application to rates for a utility not engaged in interstate

commerce and furnishing a single commodity such as gas or water. A railroad engaged in interstate commerce transports hundreds of different commodities and the rate for each article carried has a relation to all other rates and must be considered in fixing rates which will furnish a fair return.

* * * * *

If, as we contend, the power of regulation of rates by a state is limited to the prescribing of maximum rates, and that the owner of property affected with the public interest may charge rates less than just and reasonable rates, provided the same are not discriminatory, the order in question deprives the plaintiff of the liberty of contract and takes its property without due process of law, in violation of the 14th Amendment.

In the case of Lochner v. New York, 198 U. S. 45, 49 L.Ed. 937, the court said:

> "The general right to make a contract in relation to his business is part of the liberty of the individual protected by the 14th Amendment of the Federal Constitution."

In the case of Tyson & Bro. v. Banton, 273 U. S. 418, 429, which involved the constitutionality of a statute fixing the price of theatre tickets, the court, in the opinion, said:

"In the endeavor to reach a correct conclusion

in respect of this inquiry, it will be helpful, by way of preface, to state certain pertinent considerations. *The first of these is that the right of the owner to fix a price at which his property shall be sold or used is an inherent attribute of the property itself,* State Freight Tax Case, 15 Wall. 232, 278, 21 L.Ed. 146, 162, and, as such, within the protection of the due process of law clauses of the 5th and 14th Amendments, See Carrollton v. Bazzette, 159 Ill. 284, 294, 31 L. R. A. 522, 42 N. E. 837. *The power to regulate property services or business can be invoked only under special circumstances; and it does not follow that because the power may exist to regulate in some particulars it exists to regulate in others or in all.*" (Italics ours).

In the case of Coppage v. Kansas, 236 U. S. 1, 14, 59 L.Ed. 446, the court said:

> "Included in the right of personal liberty and the right of private property—partaking of the nature of, each—is the right to make contracts for the acquisition of property."

III.

The Commission did not apply the Principle of a fair Return in making the Order.

The Commission was without power to fix rates which are not in accord with the principle of a fair return on present value. A fair return is essential to due process of law.

In the case of Board of Public Utility Comrs. v.

N. Y. Telph. Co., 271 U. S. 23, 31, the court said:

> "The just compensation safeguarded to the utility by the 14th Amendment is a reasonable return on the value of the property used at the time that it is being used for the public service. And rates not sufficient to yield that return are confiscatory."

See also:

Bluefield W. W. & Imp. Co. case, 262 U.S. 679.

The Commission in its decision and report said:

> "*Were we to attempt to apply the principle of a fair return upon a fair value in this case, we would arrive at a manifestly exorbitant rate.*" (Italics ours.)

In the decision and report it is also said:

> "It is inevitable that two companies serving a territory that legitimately offers but enough business for one of the companies to operate on at a fair profit, will have to respectfully accept a return that will be less than a fair return under ordinary conditions." (R. 75).

It thus appears that the principles of a fair return which is essential to due process of law in the making of rates, was not followed by the Commission in making the order in question, and that it was not intended that the rates prescribed should furnish a fair return upon the property of appellee used and useful in furnishing the service. The rule of rate making used seems to have originated with the Commission.

Appellee was not responsible for the duplication of systems or for what is regarded by the Commission

as an "over-investment," and it would indeed be a harsh rule which would require appellee to accept less than a fair return which it is conceded the rates prescribed by this order will not furnish.

A rate order based upon an erroneous rule of law must be set aside.

> Tagg Bros. & Moorhead v. U.S., 280 U.S. 420, 442.

If the appellee is not entitled to protect its property and business by competition in the matter of rates, and the Commission is authorized to prescribe minimum rates, we then submit that the appellee is entitled to have such rates fixed upon the principles of rate making required by the due process of law clause of the 14th Amendment.

In the case of Atchison T. & S. F. Ry. Co. v. I. C. C., 190 Fed. 591, 594, it is said:

> "Whatever, therefore, the rights of the carriers may be to give reduced rates for the purpose of fostering a new or an established industry or for granting to it a higher measure of protection against foreign competition than Congress, through the revenue laws, has given it, no such power can lawfully be exercised by the commission."

See also:

> Atlantic Coast Line Co. v. Trammell, 287 Fed. 741;
> Southern Pac. Co. v. I. C. C., 219 U. S. 433, 55 L.Ed. 283.

IV.

Said Order is not supported by the Evidence introduced before or by the Finding of the Commission.

In fixing the rates prescribed in the order in question, the Commission first determined the present value of the system as $46,091.72 (R. 62). The Commission then found that Shelby "affords an annual consumption of approximately 120,000,000 cubic feet of gas," basing this finding upon the amount of gas sold by appellee before the Citizens Gas Company had entered the field as a competitor. (R. 76). The Commission proceeded to determine the cost per thousand cubic feet of supplying this amount of gas to the people of Shelby, and based the rates in question upon this cost and upon the assumption that the appellee would continue to sell this quantity of gas. (R. 76). This assumption, of course, was wholly unwarranted as the appellee had 485 customers when the Citizens Gas Company commenced operations in October, 1928, and at the time of the hearing in December, 1928, 135 of these customers had become customers of the Citizens Gas Company. (Tr. p. 61). It appears that during the year 1929 the appellee sold only 73,160,500 feet of gas and that the volume sold each year has constantly decreased. (R. 93).

It would seem from the report and decision of the Commission, and from the fact that the rates prescribed are identical with the rates which were being charged by the Citizens Gas Company, at the time the order was issued, that what the Commission had in mind was not the fixing of rates for appellee, but the fixing of rates for both companies. In fact, in the brief for Appellants, on pages 35, 36 and 102, the theory upon which these rates were prescribed is now disclosed and for the first time announced. It is argued that considering the aggregate value of both utilities and the aggregate volume of sales by both utilities, the rates are reasonable. The value of the property of the Citizens Gas Company, or its operations, had never been investigated by the Commission, at the time it prescribed rates for appellee (R. 101), and therefore, there was no evidence before the Commission upon which to fix rates upon the basis of the aggregate value of the properties of the two companies at the time the order was issued.

Appellants recognize this condition but seek to supply the deficiency in proof by constructing out of the evidence taken before the trial court, four years after the issuance of the order in question, a hypothetical aggregate rate base, operations, etc., (Appellants' Brief 89-102).That this method is not worthy of

serious consideration is plain from appellants' brief:

> "* * * * there is not legal and competent evidence in the record upon which to base positive findings upon certain of these factors." (Appellants' Brief, 94).

i. e. revenues, expenses, depreciation, value of property, fair return, etc. And again,

> "While there is not competent evidence in the record upon which to predicate an absolute finding as to aggregate present fair value of the two plants or systems, *there is sufficient evidence from which an approximate idea of the claimed values* of the respective plants can be obtained." (Appellants' Brief, 98, and see Appellants' Brief, 102).

As said by this court in the case of Northern P. R. Co. v. Department of Public Works, 268 U.S. 39, 44-45:

> "An order based upon a finding made without evidence, or upon a finding made upon evidence which clearly does not support it, is an arbitrary act against which courts afford relief. * * * * It was a denial of due process."

V.

Rates in question were not prescribed in the interest of the Public but in the interest of the Citizens Gas Company.

In the complaint, in paragraph XXI, (R. p. 7), it is alleged that:

> "said order was made arbitrarily and capriciously without regard to the public interest, and

> in the interest of and for the purpose of increasing the earnings and enhancing the value of the property of the said Citizens Gas Company."

As we have already pointed out, the only complaint made to the Commission was by the Citizens Gas Company and its customers, presumably stockholders in that Company. The theory upon which the Commission asserts the right to require appellee to increase its rates is that it is to the interest of the public that appellee should earn sufficient to maintain its plant and render adequate service. (R. p. 69).

It has now been over four years since the order in question was made, and there is no evidence that the gas system of appellee has not been properly maintained, or that the service furnished has been in any sense inadequate, or that there has been a single complaint made. It would seem that until the system of appellee is not properly maintained, or the services inadequate, or there is some complaint by the public, the theory advanced does not warrant the Commission in requiring an increase in rates.

As we have already argued, it is wholly immaterial to the consumers whether loss of revenue which may result in failure to properly maintain the system or in poor service is due to low rates or loss of patronage, and where as conclusively shown in this case an increase in rates would through a loss in patronage de-

crease the revenues, the order in question can only result in benefit to the Citizens Gas Company by destroying the business and property of its competitor. We believe it is a fair deduction from the conceded facts in this case that this order was not made in the interest of the public but in the interest of the Citizens Gas Company as alleged in the bill of complaint.

VI.

Rates prescribed by the Order are insufficient to furnish Appellee a fair return.

In the case of McCardle v. Indianapolis Water Co., 272 U. S. 400, 408, this court said:

> "In every confiscation case, the future as well as the present must be regarded. It must be determined whether the rates complained of are yielding and will yield over and above the amounts required to pay taxes and proper operating charges, a sum sufficient to constitute just compensation for the use of the property employed to furnish the service; that is, a reasonable rate of return on the value of the property *at the time of the investigation and for a reasonable time in the immediate future.*" (Italics ours).

In challenging the rates involved in this case, we are not questioning the findings of the Commission as to the value of the property, operating expenses, depreciation allowed, or rate of return to which the appellee is entitled as determined by the Commission.

What we are contending is that the rates prescribed were insufficient at the time and ever since have been insufficient to furnish the return which the Commission decided was a fair return. (R. 76-77).

In the decision and report of the Commission it is said:

> "What rate of return such a schedule will yield under the competitive conditions now existing at Shelby will largely depend upon the ability of the management to attach new customers, increase consumption among present consumers and to effect such economies in operation as are consistent with adequate service." (R. p. 77).

It is also said:

> "Were we to attempt to apply the principle of a fair return upon a fair value in this case, we would arrive at a manifestly exorbitant rate." (R. 75).
>
> "It is inevitable that two companies serving a territory that legitimately offers but enough business for one of the companies to operate on at a fair profit, will have to respectfully accept a return that will be less than a fair return under ordinary conditions." (R. 75).

As the Commission concedes that the rates prescribed will not furnish a fair return and were not intended to do so, it should not be necessary for the court to look further for support of the contention that the rates are confiscatory.

It is conclusively shown by the testimony of the witness Foster (R. 83 et seq.) and appellee"s Exhibit

5 (R. 92-93) that if the rates prescribed by the Commission had been applied to actual sales of gas from 1928 to July 1st, 1932, the revenues produced would have been insufficient to pay for the gas purchased by appellee and actual operating expenses notwithstanding there has been a considerable reduction in such expenses each year as appears from appellee's Exhibit 3 (R. 92-a).

This evidence is not controverted but evidence was introduced for appellants showing the experience of the Citizens Gas Company during said period (R. 103-110), and it is argued therefrom that the expenses of appellee could have been materially reduced.

It appears that the Citizens Gas Company is a one-man company so far as operation is concerned. The witness Tillman is the manager, secretary and treasurer, and has a 1/8 or 1/9 interest in the company. (R. 108). He receives a salary of $300.00 per month (R. 107). The company does not pay office rent but is permitted to use the building of the manager, who is engaged in the plumbing business. (R. 106). The manager provides a bookkeeper and maintains the plant. (R. 107). The manager also reads the meters, and if any one is employed to do this work, payment therefor is made by the manager out of his salary. (R. 108). The Citizens Gas Company has

paid no federal income tax in the years 1929, 1930, or 1931. (R. 106).

The witness Tillman testified that the total revenues for 1929 were $21,675.24. (R. 106). Total expenses including cost of gas and depreciation was $20,190.49. (R. 106). The item of revenues represented the charges and not the actual collections. (R. 108).

If the Citizens Gas Company had been required to pay 7 cents per M. cubic feet of gas, the amount paid by appellee, instead of 3 cents per M. cubic feet, the rate paid by that company (R. 106), there would have been no return whatever, but a deficit.

Sufficiency of Complaint

It is contended for appellant that the complaint does not present an issue of confiscation because of insufficiency of rates to furnish a fair return.

On the hearing of the application for an interlocutory injunction this same contention was made, and in the concurring opinion of Judge Sawtelle it is said:

> "The defendant commission contends that the plaintiff is not in position to urge the question of confiscation because the complaint does not present the issue, and, secondly, because there is no evidence as to the present fair value, fair rate, etc. The complaint, however, in paragraph XX, does specifically invoke the due process of law clause of the Fourteenth Amendment; and

> the order, on its face, shows that the 'fair return' rule was consciously and deliberately disregarded by the commission. There is, consequently, no need of further evidence on the subject. The report itself is the best evidence." 52 Fed. (2d) 802.

At the final hearing an amendment to the complaint was proposed, alleging that the rates are insufficient to furnish a fair return and if made effective would deprive appellee of its property in said gas system without due process of law in violation of the Fourteenth Amendment. (R. 114). The proposed amendment was said by the trial court to be unnecessary and was disallowed. (R. 23).

As before stated, appellee makes no complaint of the findings of the Commission as to value, etc., but bases its contention of confiscation upon the ground that the rates are insufficient to furnish a fair return.

There was, therefore, no occasion to make any allegations with reference to value, expense of operation, depreciation, or rate of return, and it is clearly alleged in paragraphs XX and XXI of the complaint that the rates are not supported by the evidence, and if adopted would deprive appellee of its property without due process of law, which is the equivalent of an allegation that the rates are insufficient to furnish a fair return.

The statement in paragraph XXI that there is no evidence showing, or tending to show, that the rates are reasonable or just, is clearly the statement of an ultimate fact, as required by Equity Rule 25, and presents the issue of whether the findings made by the Commission sustain the rates prescribed by this order.

The only purpose of introducing any testimony was to show the effect of said rates from experience and sustain the charge that they were insufficient to furnish a fair return upon the value of the property as fixed by the Commission.

As said in the case of Smith v. Illinois Bell Tel. Co., 282 U. S. 133-160, "In determining what is confiscatory regulation of rates, it is necessary to consider the actual effect of the rates proposed in the light of the utilities situation, its requirements and opportunities."

Contention for Appellants that Franchise Contract precludes Appellee from challenging Rates in Question.

Section 3 of the ordinance granting the franchise, pursuant to which the gas system of appellee was installed and is being operated provides:

> "The rates to be charged for gas of whatsoever kind and the regulations governing such service shall be such as the Board of Railroad Commissioners of Montana shall order and determine."

The contention is made in behalf of the appellants that by virtue of this provision of the franchise contract, appellee is required to accept the rates in question. (Appellants' Brief, 69-70). It seems unnecessary to make any answer to this contention. This provision, of course, assumed that the rates would be legal rates, such as were within the power of the Commission to prescribe, and not violative of the due process of law clause of the Fourteenth Amendment.

Insufficiency of Findings

It is argued that finding No. 4 (R. 24) is insufficient because of failure to find present value and make other findings required in prescribing rates which will furnish a fair return. What has been said with reference to the sufficiency of the complaint applies equally to the objection to this finding. The court was not required to find what the Commission had already found when there was no controversy over the findings made by the Commission. The question presented was whether the rates prescribed will furnish a fair return in view of the facts as found by the Commission. The finding by the court is of an ultimate fact that such rates will not furnish a fair return.

* * * * *

We are surprised to note the statement in Appellants' Brief, page 89, that the Commission did not

make a finding of what would be a reasonable rate of return. In the report and decision of the Commission (R. 76), it appears that the Commission found that "the cost of gas purchased and cost of doing business, when translated into cost per thousand cubic feet of gas sold amounts to 21.32 cents." There was included 2.82 cents per M. cubic feet of gas sold as an allowance for depreciation. It is said:

> "Rate of return at 8 per cent on the present value of the utility's property amounts to $3,687.33, or about 3 cents per M. cubic feet of gas sold. Aggregating the above costs per thousand cubic feet of gas sold, it appears that a schedule of rates that will yield an average revenue of 27.13 cents per M. cubic feet sold would, under ordinary circumstances, represent a schedule of rates that is capable of earning enough revenues to pay all operating expenses, including depreciation, and a fair return upon the value of property necessarily required to render adequate natural gas service to the consumers of Shelby." (R. 76).

If the Commission did not find that 8% would be a fair return, why were rates prescribed which the Commission assumed would furnish such a rate of return?

The decree should be affirmed.

Respectfully submitted,

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